



## **Report to the Secretary of Defense**

# **Task Group on Best Practices for Export Controls**

### Report FY09-3

- **Recommendations to improve export control rules and processes based on commercial best practices of the United States and those of foreign governments.**

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**October 2008**

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## Best Practices for Export Controls

### TASK

This effort was initiated by the Under Secretary of Defense, Acquisition, Technology, and Logistics (USD(AT&L)) who, after facing increasing criticisms for slow and unnecessary “red tape” procedures that inhibit critical business opportunities for both the U.S. and its allies, requested help from the Defense Business Board (DBB) for ideas and recommendations to help improve the processes and practices used by the Department of Defense (DoD).

In response to the USD(AT&L)’s request, the Deputy Secretary of Defense tasked the DBB to form a Task Group to review current practices regarding export controls rules and processes; and to identify export control best practices by foreign governments and commercial best practices in the United States (U.S.). The Task Group was asked to provide the Department with recommendations on lessons learned and best practices from the U.S. commercial sector and foreign governments that could improve DoD’s policies and practices. A copy of the official Terms of Reference (TOR) may be found at **Appendix A**.

The Task Group was chaired by Mark Ronald and supported by Mel Immergut, Bill Phillips and Atul Vashistha. The Group was assisted by DBB consultants, Pierre Chao, Steven Price and Alan Schwartz. The Task Group Sponsor was John Young, Under Secretary of Defense for Acquisition, Technology and Logistics (USD(AT&L)). The Task Group Executive Secretary was Kelly S. Van Niman, DBB Deputy Director.

### BACKGROUND

The U.S. export control system is managed by two federal agencies: the Department of State for defense items and the Department of Commerce for dual-use items. Both federal agencies refer to DoD for support and input on questions pertaining to classification and jurisdiction.

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Within the DoD, the Under Secretary of Defense for Acquisition, Technology and Logistics (USD(AT&L)) is responsible for the policies and procedures for technology transfers as administered by the Director of International Cooperation. Additionally, the Defense Technology Security Administration within the office of the Under Secretary of Defense for Policy (USD(Policy)) reviews the controlled items from a policy perspective. This report focuses on the overall U.S. system for export controls and on DoD's role in that process, and contains recommendations intended to help improve the policies and practices in the overall export controls process.

### **PREMISE**

The Task Group began their study with the premise that the U.S. export control system is fraught with processes developed in the post-World War II and Cold War eras and, in today's global economy, those processes are causing lengthy review times and prompting slow decision-making. Slow decision-making has a negative impact on the U.S. private sector and foreign governments who desire to trade technology and defense items with the U.S. The Task Group believes that the current U.S. export control system needs improvement to reduce these inefficiencies (i.e., reduce unnecessary volume and increase the speed of decision-making) while maintaining necessary security policy objectives.

The Task Group recognizes that export controls are an important tool of U.S. national security and that sustaining U.S. technological superiority continues to be a critical component of U.S. military strategy. Therefore, protection of items that give the U.S. military a "battlefield advantage" cannot be sacrificed for efficiency. Additionally, the Task Group understands that because technology continues to diffuse around the world, any effective export control system must be agreed to and executed in concert with the U.S.'s major allies and other weapons exporting nations.

The Task Group supports the philosophy that trade-offs of best practices must distinguish between effectiveness and efficiency, with emphasis on effectiveness.

## PROCESS

In addition to relying on their own professional expertise obtained from dealings with the U.S. export controls system, the Task Group interviewed past senior leaders who have dealt with the DoD rules and processes, and held several informational briefings and meetings with DoD leaders responsible for DoD's rules. The Task Group also conducted outreach to foreign countries for insights into their own processes and experiences in dealing with the U.S. processes.

The Task Group began the study with an overview session with the Defense Technology Security Administration (DTSA) from the OUSD(Policy) and the Office of International Cooperation from within the OUSD(AT&L) to obtain a better understanding of the role played by each organization within DoD. Members of the Task Group also attended the Center for Strategic and International Studies' conference "Toward a 21<sup>st</sup> Century Export and Technology Control Regime" to listen to the latest best practices trends in the international community.

The Task Group reviewed the rules and processes of fifteen foreign countries by collecting information from two sources: (1) conversations with the office of the Director of International Negotiations, OUSD(AT&L), and (2) voluntary surveys of the foreign Defense Military Attaché Group located in the Washington D.C. area. Between the two sources, the Task Group reviewed export controls rules and processes in following countries:

Foreign Countries Reviewed	
Finland	Portugal
Canada	Czech Republic
France	Germany
Israel	Italy
Japan	Korea
Poland	Singapore
Spain	Sweden
United Kingdom	

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Of the foreign countries reviewed, six are European Union (EU) countries, one a Middle Eastern ally, and three Asian governments. The countries surveyed are either members of the four major international nonproliferation regimes or are adherents (i.e., the Australia Group, the Missile Technology Control Regime, the Nuclear Suppliers Group, and the Wassenaar Arrangement). Only two non-NATO allies are not formal parties of any international regimes.

The Task Group also developed interview questions to help guide their information gathering and discussions with global companies headquartered in the U.S. who routinely deal with export controls in their global business sectors.

The Task Group presented their findings and recommendations to the full Board on October 23, 2008. A copy of the briefing containing the final recommendations as approved by the Board at the meeting may be found at **Appendix B**.

## OBSERVATIONS

The Board's observations are categorized according to foreign governments, U.S. commercial sector, and lastly, a comparison between U.S. government rules and foreign government and commercial best practices.

### Foreign Governments

No country-to-country consistency was observed with regard to the lead agency designation or weighted ministry input. In most cases, an economics-oriented ministry is the lead agency and in only two non-EU countries is the Ministry of Defense the lead agency.

The Board observed that, like the U.S., the foreign countries have multiple cabinet-level agencies that have important influence and/or authority in export licensing decisions, even if they are not the lead agency. For example, the Ministry of Foreign Affairs plays an influential role in these decisions in all of the countries reviewed but one. Additionally, in 70% of the countries reviewed, the Ministry of Defense is involved in decisions.

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The Board also observed that the Wassenaar Arrangement requires participating states to control software or source code in all the control categories.

The Board noted many similarities between the foreign countries surveyed and the U.S. regarding systems and organizational approach to manage the release of technology. However, none of the surveyed countries review the same volume of license applications as the U.S. screens. For example, foreign countries might review between 5,000 to 8,000 licenses per year, whereas the U.S. reviewed 38,000 licenses for dual-use and munitions in 2007 alone.

The Board observed three key best practices used by foreign governments; (1) for weapon systems intended for export, their early and frequent interaction with industry and embedded in the design phase from inception, (2) their strong commitment to design an export control regime guided by the philosophy that it is more effective and efficient to “build higher walls around a smaller list of items,” and (3) their senior leadership commitment to strive for interoperability among allies through bilateral and multi-lateral agreements, (e.g., the European Union Code of Conduct).

A clear commonality seen between foreign government practices and the commercial sector was how companies develop multiple versions of products to protect their intellectual property and still allow for global sales.

### **U.S. Commercial Best Practices**

Like the foreign governments, U.S. industry considers it a critical best practice to develop multiple versions of products to protect intellectual property and facilitate global sales. This practice is essential to conduct international transactions in both the commercial and government sectors.

U.S. companies tend to reassign the ownership/control of their intellectual property to the entity with the most favorable benefit. For example, companies will “spec out” components controlled under the International Traffic in Arms Regulations (ITAR) and/or move development of the technology overseas to avoid ITAR regulations.

Most importantly, U.S. companies centralize the management of export controls and technology transfer procedures and use automated processes to maintain smooth, credible and reliable processes. U.S. companies also will ensure that technically qualified individuals make the decisions regarding technology transfers to commercial partners. They also integrate export control experts into their development teams from the beginning of a development program, where it matters most, and during cooperative development projects.

Additionally, U.S. companies focus on annual training to ensure that their technical experts maintain a current and thorough understanding of technology transfer rules. Technical experts are guided by senior-level policy and precedence when pre-clearance is given for like-sales and other day-to-day technology release decisions. To help validate compliance and track training, corporate executives conduct quarterly reviews and maintain scorecards reflecting the results of the reviews. The scorecards are distributed throughout the organization to provide visibility and help improve these processes.

Through internal automated controls, U.S. companies routinely require an internal certification that export control procedures have been completed before the technology is released. Companies also continuously review and leverage new technologies to help improve their automated approval procedures to help speed decisions, minimize mistakes, and ensure clear hierarchy for access and visibility.

#### A Comparison of U.S. Government Rules to those of Foreign Government and U.S. Commercial Best Practices

When assessing the practices of foreign governments and the U.S. government, the Board discovered that in addition to their intended purpose, foreign governments will use export controls policies for secondary purposes such as to bolster their foreign or economic policy initiatives. For example, a country whose primary objective is to bolster their economy will have a more user-friendly export control system that will not hinder potential economic growth.

However, because U.S. has the “most to lose,” with its larger arsenal of arms and high-tech technological weapon systems, its export control



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system is most oriented toward preventing unauthorized release of sensitive technology. Additionally, whereas allies note that exports are important to maintaining their industrial base, U.S. defense exports are not as critical to maintaining a strong industrial base.

The U.S. government does not consider exports as a primary factor in most technology development programs, and therefore exportability and/or technology transfer issues are not considered in the original design or at least with rare exception. These key differences lead to the U.S. having a stricter system and looking at every export destination as a potential risk.

The Board observed that tactical improvements to the overall U.S. system would be difficult given the bifurcated U.S. system between the Department of Commerce for dual-use items and the Department of State on military items, and the resulting inter-agency rivalries that arise within both agencies. The process is further complicated when disagreements from both agencies arise when referring questions to DoD.

The Board noted that the U.S. government rarely changes or updates the ITAR and hence it often does not keep pace with technological advancements and/or global availability. This situation, coupled with the Pentagon's and Congress' tendency to reverse policy direction by cutting funding for a project, results in the U.S. often being seen as an unreliable partner in bi-lateral and multi-lateral cooperative development projects.

## **RECOMMENDATIONS**

Based on the observations above, the DBB offers the following six recommendations.

1. Considering the rapid pace of technological change and in order to have a more effective export control system focused on critical technologies, the Board recommends that the Secretary of Defense set a 90-day deadline to obtain agreement of inter-agency counterparts to annually update the U.S. munitions list. Additionally, the Board recommends that particular attention be given to modifying the list for dual-use and other commercially derived items. To gain the insights from cutting edge scientific and/or technical experts, the U.S. should consider using the Defense Trade Advisory Group

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(DTAG), or a subcommittee thereof, to make independent recommendations on an annual basis on which items to include on the munitions list and dual-use items list.

2. Recognizing that the Department does not have the lead, nonetheless, the Secretary should advocate to his counterparts at State and Commerce an export controls policy that focuses on enforcement with appropriate controls related to critical technologies. Where possible, DoD should seek to expand the use of broader technology sharing agreements with close allies and use broader program licenses more often for programs that include subsystems and spares to reduce volume.

3. To help facilitate Recommendation 2 above, the Secretary should issue clear internal policy guidance for defense sales to particular countries, and discontinue its current transactional approach, that lacks transparency to the country and industry, and often results in treating allies as foes.

4. Given the importance of enhancing partnership capacity, facilitating the U.S. military's interoperability with allies and sustaining critical capacity within the defense industrial base infrastructure, the Department must advocate legislative change necessary to achieve these goals. The Board recognizes the lead role of the Departments of State, Commerce, and to a lesser degree Treasury, and recommends that the Secretary lead a legislative outreach program in coordination with the aforementioned Departments to inform Congress about global technology trends of defense-related items and modified commercial items.

5. Consistent with the best practices by foreign governments and the commercial sector, the Board also recommends that the Secretary work to help sustain the industrial base infrastructure by working closely with industry to identify those items where export will be necessary. Additionally, to enhance partnership capacity and improve interoperability with allies, the Secretary should establish a revolving fund to pay for the development of an exportable version of appropriate items developed in DoD's acquisition programs. The Secretary should consider using Foreign Military Sales dollars as seed money for such a program, and work closely with industry to identify those items where export will be necessary.

6. Lastly, the Secretary should continue to streamline the export control/technology transfer organizational structures within the Department and speed decision-making by automating standardized export reviews and aligning the organizational structure with the bulk of technical expertise.

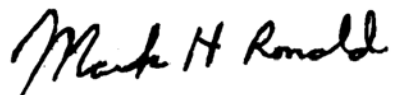
## CONCLUSION

The Board advises the Secretary and Deputy Secretary of Defense to convey this critical advice to their successors, who will have a unique opportunity to improve the effectiveness and subsequently the efficiency of the U.S. export control system. Specifically,

1. The Senior DoD leadership should share the recommendations of this report with:
  - The Presidential Transition teams
  - Industry (industry meetings, trade associations, etc.)
  - The Congressional committees of jurisdiction
2. The next Administration should develop a one-year implementation plan.

The Board recognizes that because the U.S. has the most to lose if its technology were diverted to an unintended end-user, the protection of items that give the U.S. military a battlefield advantage cannot be sacrificed for efficiency. Nonetheless, the Board is hopeful that the Secretary will find these recommendations helpful toward achieving greater transparency and focus in its export control policies and system, and that implementation of these recommendations will help the Department sustain critical industrial base infrastructure, enhance partnership capacity, and improve interoperability with allies.

Respectfully Submitted,



Mark H. Ronald  
Task Group Chairman

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**APPENDIX A**  
**(TASK GROUP TERMS OF REFERENCE)**

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## DEPUTY SECRETARY OF DEFENSE

1010 DEFENSE PENTAGON  
WASHINGTON, DC 20301-1010

MAR 10 2008

### MEMORANDUM FOR CHAIRMAN, DEFENSE BUSINESS BOARD (DBB)

SUBJECT: Terms of Reference - DBB Task Group on Best Practices on Export Controls

Due to the increasing globalization of the defense industry, request you form a Task Group to review best practices regarding export control rules and processes. Specifically, the Task Group should: (1) examine export control rules in other countries, (2) identify commercial best practices in the United States, and (3) assess the United States rules as compared to both commercial best practices and practices in other countries.

The Undersecretary of Defense for Acquisition, Technology and Logistics will be the DoD Liaison. The DBB will form a Task Group and name a Chair and Executive Secretary within the coming week. The Task Group will plan its actions to present recommendations no later than the July 2008 quarterly meeting.

The Task Group will be operated in accordance with the provisions of P.L. 92-463, the "Federal Advisory Committee Act," and DoD Directive 5105.4, "the DoD Federal Advisory Committee Management Program." It is not anticipated that this Task Group will need to go into any "particular matters" within the meaning of Section 208 of Title 18, U.S. Code, nor will it cause any member to be placed in the position of acting as a procurement official.



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**APPENDIX B**

**(TASK GROUP FINAL REPORT – OCTOBER 23, 2008)**

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# Task Group on Best Practices on Export Controls

Final Report

October 2008



# Task Group

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## Sponsor

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## Task Group Executive Secretary

Kelly S. Van Niman, DBB Deputy Director



## Deliverables

- Review current best practices regarding export controls rules and processes and identify
  - Export control best practices by foreign governments
  - Commercial best practices in the United States (U.S.)
  - Assessment of the U.S. rules as compared to both commercial best practices and best practices by foreign governments
- Recommend lessons learned/best practices from foreign governments and/or the commercial sector that could inform DoD policy and practices



## **Premises**

- Export Controls are an important tool of U.S. national security
- Sustaining technological superiority continues to be a critical component of U.S. military strategy
  - Relies on large domestic technology expenditures and the ability to draw on raw technology from around the world
  - These technologies result in superior U.S. weapon systems in many areas of warfare
- Protection of items that give the U.S. Military a battlefield advantage cannot be sacrificed for efficiency
  - Most key technology now developed in the private sector, vice military sector
  - DoD requirements are not large enough to drive technology markets
  - Trade-offs of best practices must distinguish between effectiveness and efficiency, with emphasis on effectiveness



## Premises

- Technology continues to diffuse around the world
- The strategic goals of an export control system can only be achieved if agreed to/executed in concert with our major allies and other weapons exporting nations
- Current system is in need of improvement to reduce inefficiency (reduce unnecessary volume and increase speed of decisions)
  - Current regulations written for post-WWII/Cold War industrial environment
  - Volume of export licenses continues to increase significantly



## **Export Control Systems of Foreign Governments**

- Survey of key countries around the world – 6 EU countries (5 NATO), 1 Middle East ally, 3 Asian allies found that all have export control systems based in legislative statute
- All countries surveyed are either members of the four major international nonproliferation regimes or are adherents (Australia Group, the Missile Technology Control Regime, the Nuclear Suppliers Group, the Wassenaar Arrangement) – two non-NATO allies are not formal parties
- There is no country-to-country consistency in lead agency designation or weighted ministry input
  - In only two non-EU countries is the Ministry of Defense the lead agency
  - In most other cases an economics-oriented ministry is the lead agency
  - Economics drive more joint development programs with allies and need to export





## **Export Control Systems of Foreign Governments**

- Multiple cabinet-level agencies in surveyed countries have important influence and/or authority in export licensing decisions, even if they are not the lead agency
  - Ministry of Foreign Affairs has a say in all countries but one
  - Ministry of Defense involved in 70% of the countries
- Surveyed countries do not have the volume of license applications that the U.S. screens
  - Others in the 5-8,000 licenses a year versus
  - U.S. in 2007 had over 38,000 licenses (munitions/dual-use)
- Wassenaar Arrangement requires participating states to control software or source code in all of the control categories



## **Export Control Best Practices by Foreign Governments**

- Early and frequent interaction with industry to develop defense articles mindful of the global stakeholders/buyers
  - Design exportable version from inception
- Design export control regime guided by the philosophy that it's more effective and efficient to "build higher walls around a smaller list of items"
- Senior leadership strive for interoperability among allies through bilateral and multi-lateral agreements, i.e., the European Union Code of Conduct



## **Commercial Best Practices in the U.S.**

- Companies develop multiple versions of products (to protect their intellectual property) for global sale
- Companies reassign the ownership/control of their intellectual property to the entity with the most favorable benefit
  - Companies “spec-out” components controlled under the International Traffic in Arms Regulations (ITAR) and/or move development of the technology overseas to avoid ITAR
- Companies working together on co-development, grant no-fee cross-licensing agreements for their technology
- Centralize management of export controls/technology transfer
  - Ensure that technically qualified individuals make the decisions
  - Integrate export control experts with development teams from the beginning



## **Commercial Best Practices in the U.S. (continued)**

- Provide annual training to ensure thorough understanding/transparency of technology transfer rules
  - Guided by senior-level policy and precedence – pre-clearance given for like-sales
  - Technical experts make day-to-day technology release decisions
- Leverage new technology to ensure clear hierarchy for access/visibility
  - Require internal certification that export control procedures have been completed before technology release
  - Automate standardized exports approvals to speed decisions and minimize mistakes
- Maintain quarterly scorecards to validate compliance and track training
  - Scorecards are distributed throughout the organization and reviewed by the executive staff



## **Assessment: US Rules vs. Foreign Government and Commercial Best Practices**

- Because U.S. has the “most to lose”, the system is most oriented toward preventing unauthorized release of sensitive technology
- Allies note that exports are important to maintaining their industrial base. U.S. defense exports are not as critical to maintaining a balance of trade – and therefore U.S. has a stricter system
- U.S. does not consider exports as a primary factor in most development programs, therefore exportability and/or technology transfer issues are not considered in original design (with rare exception)
- U.S. looks at every export destination as a potential risk – even our closest allies
- U.S. and many foreign governments use export controls/technology transfer policies to promote foreign policy objectives



## **Assessment: US Rules vs. Foreign Government and Commercial Best Practices (continued)**

- Bifurcation of U.S. system between dual use and munitions items, and resulting inter-agency rivalries, make tactical improvements difficult
- U.S. does not frequently update its list of controlled items, keeping pace with technological advancements and/or global availability
- U.S. often seen as unreliable partner in bi/multi-lateral co-development
  - Role of Congress (ability to cut program funding) is unique to U.S. and is often underestimated by foreign governments, particularly those with parliamentary systems
    - Pentagon's commitment to international programs has varied over the long term



## Recommendations

1. Considering the rapid pace of technological change and in order to have a more effective export control system focused on critical technologies, the Secretary should set a 90-day deadline to obtain agreement of inter-agency counterparts to annually update the U.S. munitions list
  - a) Particular attention must be given to modifying the list for dual-use and other commercially derived items
  - b) Consider using the Defense Trade Advisory Group (DTAG) to make independent recommendations on an annual basis on which items to include on the munitions list and dual-use items list
    - 1) Create a subcommittee under the DTAG with members who have cutting edge scientific and/or technical expertise



## **Recommendations (continued)**

2. The Secretary should advocate to his counterparts at State and Commerce an export controls policy that focuses on enforcement with appropriate controls related to critical technologies – emphasize enforcement with new allies
  - a) Expand the use of broader technology sharing agreements with close allies
  - b) Use broader program licenses more often for programs that include subsystems and spares to reduce volume
3. The Secretary should issue clear internal policy guidance for Defense sales to particular countries
  - a) Discontinue current transactional approach, that lacks transparency to the country and industry, and often results in treating allies as foes





## **Recommendations (continued)**

4. The Secretary should lead a legislative outreach program (in coordination with the Departments of State, Commerce, Treasury) to inform the U.S. Congress about global technology trends of defense-related items and modified commercial items
  - a) Advocate legislative change where necessary to enhance partnership capacity, facilitate the U.S. military's interoperability with allies and sustain critical defense industrial base infrastructure



## **Recommendations (continued)**

5. The Secretary should establish a revolving fund to pay for the development of an exportable version of appropriate items made under Defense acquisition programs
  - a) Use Foreign Military Sales dollars as seed money
  - b) Work closely with industry to identify those items where export will be necessary, e.g., to sustain industrial base infrastructure; enhance partnership capacity; improve interoperability with allies
6. The Secretary should streamline the export control/technology transfer organizational structures within the Department of Defense
  - a) Speed-up decision-making – automate standardized export reviews
  - b) Align the organizational structure with the bulk of technical expertise



# NEXT STEPS

1. The Secretary of Defense and Deputy Secretary of Defense should convey this critical advice to their successors
2. The Senior DoD leadership should share the recommendations of this report with:
  - The Presidential Transition teams
  - Industry (industry meetings, trade associations, etc.)
  - The Congressional committees of jurisdiction
3. The next Administration should develop a one-year implementation plan

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